

Weekly Review<?xml:namespace prefix = o

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It would be an understatement to say it was a dismal week for precious metals investors (except for those looking to buy) as gold and silver prices fell nearly every day back to the lows of the mid-April price smash. For the week, gold fell a sharp \$88 (6.1%) and silver finished down \$1.60 (6.7%). As a result, the silver/gold ratio widened out a bit to just over 61 to 1, still within the broad trading range of the past month and year.

It is small consolation that silver has held up relatively well compared to gold on the downside, as overall losses to investors have been too great as to even bother to make such distinctions. When the selling carnage is over (and it will be over at some yet to be determined point) silver should lead the way higher for a variety of reasons, but the issue at hand is getting the price decline over with. I'll deal with the prospects for that later, but let's run through the normal review first.

Like a record stuck in a groove, the frantic turnover in the COMEX-approved silver warehouses continued as it has for the past two years. This week, overall movement into and out from these warehouses came to around 3.5 million oz, as total inventories declined 1.5 million oz to 164 million oz. As has been the

case for these past two years, I am more concerned with the movement rather than the totals as it is the movement that indicates tight supply conditions to me.

I don't think for a moment when we experience weekly declines in COMEX silver (or gold) inventories that means the metal no longer exists; I know it has just been shipped to a different location. That such a large percentage of world daily production and consumption of silver has been moved so consistently for such a long time (coinciding with the first real signs of a physical silver shortage in April 2011) in COMEX warehouses begs the question why. That this movement is not apparent in any other metal adds to the question. My best guess is hand to mouth tightness and general unavailability of the bulk of COMEX inventories at current prices.

The last few days has seen the big silver ETF, SLV, join with its gold counterpart, GLD, in a notable liquidation of metal holdings of some 6 million oz. This follows a long stretch of no metal liquidation in SLV, despite persistent price weakness since the beginning of the year. As it stands, silver holdings in SLV are still slightly higher year to date, whereas holdings in GLD are down close to 25%. Based upon the normal delays in SLV holdings and the pronounced weakness in silver prices over the past three days, more liquidation seems likely. I'd like to tie this in with some general comments later, so I ask your patience.

Sales of Silver Eagles from the US Mint still seem constrained by silver blank supply, based upon the Mint's previous statement that they could produce as many as 5 million coins per month if blank supply were readily available. This is based upon the last report of sales earlier in the week, as reporting from the Mint is still somewhat erratic. Premiums may have cooled off a bit (from extremely high levels) but I think it is fair to say that the Mint would be selling more Silver Eagles if they could produce them. Of course, retail demand is different from wholesale demand (as measured by COMEX warehouse movements). I don't sense that the Mint is having problems producing Gold Eagles, despite its suspension of sales of one-tenth oz coins. And none of this has anything to do with foreign physical demand for silver and gold, which appears strong. Then again, I don't think foreign physical demand has much to do with current price movements for gold and silver. As is usually the case, activity on the COMEX is the prime determinant for gold and silver price moves.

This week's Commitment of Traders Report (COT) came in largely as expected in that there was some slight improvement (reduction) in the headline total commercial net short position for both gold and silver. Through the cut-off on Tuesday, gold had been down around \$25 and silver off by maybe 50 cents on generally lackluster trading volume, so the modest reductions made sense. Since the cut-off, however, prices of each were hammered (gold by \$65 and silver by more than a dollar) on heavy volume so I would expect significant

further reductions in the commercial net short positions of perhaps 20,000 contracts in gold and 5000 in silver through the close on Friday.

In gold, the total commercial net short position declined by 3600 contracts (thru Tuesday) to 84,100 contracts, another new low going back to 2008. By commercial category, there was a bit of a mix from the past couple of weeks, as the big 4 and big 5 thru 8 bought back 5500 and 2400 contracts each and the raptors sold off 4300 contracts of their record net long position. The raptors are still holding 42,800 gold contracts net long, their largest long position ever, save for last week. And there has been only one other occasion in the past 5 year or so, that the big 4 have been less net short than the 83,000 contracts they hold now (thru Tuesday). Regardless of what prices do in the short term, these are strongly bullish readings.

Under the hood, there were some interesting details in the gold report. For one thing, I don't recall a report in many years (if ever) where the concentrated holdings of the 4 largest traders on the long side of gold were larger than the big 4's concentrated short position, as was the case this week. By process of elimination, it appears that a big long position has emerged in the producer/merchant category of the disaggregated report, the category which includes JPMorgan. Thus, I think JPMorgan has flipped to the net long side in COMEX gold futures, perhaps for the first time in many years. I'll tie this in with some general comments in a moment.

Another interesting development was the reemergence of the technical funds (managed money category) as big net sellers, both in long liquidation and new short selling. In fact, the net selling by the tech funds was more than 9000 contracts, much more than the 3600 contract headline improvement. In the process, the tech funds have established a new record short position on a gross contract basis. I would imagine the tech funds added to that short position over the past few days and that could serve as buying fuel to the upside when the turn in price comes.

In silver, the total commercial net short position declined by 1200 contracts to 13,200 contracts, another recent new low going back to December 2011 and last summer. If the commercials bought as much as I think they did in the past few days, the commercial net short position would be at lows not seen in a decade and perhaps much longer than that. By commercial category, it was mainly a raptor (the smaller commercials apart from the big 8) affair, as they bought an additional 1900 contracts, increasing their net long position to another new record of 35,100 contracts. The big 4 (read JPMorgan) added 500 contracts and the big 5 thru 8 added 200 new short contracts as well.

The record silver raptor net long position (as well as the near record gold raptor net long position) most likely increased after the cut-off, as did the big 4 short

position decline. It does appear likely to many that prices will decline further for silver and gold, but I am hard-pressed to see significant quantities of speculative selling still to come. Like in gold, the technical funds (in the managed money category of the silver disaggregated COT report) sold much more (almost 3000 contracts) than the headline 1200 contract improvement. Almost of that selling was in the form of new short sales, providing potential buying firepower on a price turn. I would guess that the tech funds sold even more short over the past few days in silver. I know that these tech fund short sellers made out like bandits in the two-day April smack down, but it remains open as to whether they can pull that off again.

JPMorgan appears to still hold 18,000 to 18,500 contracts of COMEX silver net short, the same amount as the past few weeks, as the raptors have been the big commercial buyers. I would imagine JPM has reduced their silver short position in the past few days, but even if they haven't it may not matter much. For all intents and purposes, I feel JPMorgan has, effectively, covered its concentrated silver short position in a variety of ways. Those ways include buying real silver (thru the SLV) and in OTC derivatives dealings, as well as buying COMEX and OTC gold contracts and gold itself (thru the GLD). One can never be sure of the precise price bottom or point at which outside forces of selling will dry up, but considering the staggering amounts of different items that JPMorgan appears to have bought in the sell-off, we must be closer to the point of selling exhaustion than ever before.

It is important to remember that in every single transaction there is a buyer and seller and there are no exceptions, regardless if the transactions involve stock, metal or derivatives contracts. There is no question that over the past few months we have seen tremendous selling in gold, in particular, and in silver as well on the sharp price weakness since the beginning of the year. This is easily confirmed in the public data available, namely, COT data and ETF statistics. It is reasonable to assume the same pattern of heavy selling has occurred in markets not easy to verify, such as OTC derivatives dealings. If many entities are selling in the markets that can be verified because of declining price, most likely these and other entities are also selling for the same reason in the markets that can't be documented.

In virtually all the media reports I read about the precious metals sell-off, all point to the avalanche of selling in terms of who is selling. Almost none of the media reports mention who the buyers may be, although it is axiomatic that there must be a buyer for every seller in every transaction. Generally, when most media reports focus on just one side of a story, there is generally a distortion in the reporting. I think that's the case here. The overwhelming obsession with who's on the sell side with no mention of the buyers is a distortion. That's where the COTs and other verifiable data come in.

We know for a fact that on the price decline in gold and silver that the sellers have been the speculators, both liquidating long positions and establishing new short positions. We know that the buyers have been the big commercials, led by JPMorgan, both in closing out short positions and establishing new long positions. Anyone with a modicum of knowledge about the COTs will verify this. There still may be some resistance to the idea that the commercials have manipulated prices lower to achieve the acknowledged results, but even that resistance is less than it has been formerly. The fact is that the COMEX commercials have bought what the speculators have sold in record amounts. The bottom line in the most documentable data source available is that the commercials have been the big buyers; this despite virtually no mention of this in media reports.

If the general public and the institutional speculative community have been the verifiable sellers on the COMEX, it follows that these same sellers have been on the sell side in ETF and OTC dealings. Therefore, the same commercial buyers have been at work in the ETFs and OTC; it really can't be any other way. The only thing left is to contemplate what happens next, after the speculative selling burns itself out, as it must at some point. Admittedly, trying to determine that precise point in advance is difficult; but leaving that aside, it is less difficult to imagine what comes next, particularly when you know who the buyers are and what they have done historically.

All this comes at a fascinating point in history. The commercials and JPMorgan have established a massive overall long position in gold and silver, just as they have succeeded magnificently in asserting their power over the regulators and the markets in other ways. I try to be objective about these things as an analyst and there should be no question that JPMorgan has crushed any attempt by the regulators to curtail their trading dominance in the world of commodities once and for all. The CFTC just passed key pieces of Dodd-Frank regarding swaps that the banks didn't object to.

<http://dealbook.nytimes.com/2013/05/16/regulators-overhaul-derivatives-market-but-with-a-caveat/> This tells us the regulations were so watered-down that it didn't bother the banks. Otherwise, the banks would have gone to court to derail it, as they did with position limits. Or, as they did with the Volcker Rule, delay it to the next millennium. The mere fact that JPMorgan allowed the vote means it already passed the bank's scrutiny.

In a perfect world, overt price manipulation would be dealt with appropriately. But we live in a world far from perfect and it is clear that there is no way that the CFTC will ever go up against JPM for the silver manipulation, or prevail even if they tried. I don't regret all the years of trying to end the silver manipulation because I think it is better that I did (always with your help) by elevating the issue along the proper lines of concentration and position limits. And I'll try to do more in the future, but not by urging or expecting the agency to do the right thing; different methods are called for.

In a real, if imperfect, world JPMorgan's ascendancy to complete dominance may not be so terrible at this time from a gold or silver investor's perspective. There may be some further rough sledding ahead in the short term as the last of the speculative selling is lured into the market, but there appears to be little likelihood that the speculative short sellers will prevail in the end against JPMorgan or the raptors. Considering that much of the existing commercial long position is under water at current prices and that the commercials are unlikely to sell until they have a profit that implies we have to move some distance up in price until all positions are profitable. In the case of the silver raptors, that still looks like \$30 or more.

If I am correct in my assumption that JPMorgan has established big long gold positions in COMEX futures, actual metal and gold derivatives as a hedge against their remaining COMEX silver short positions, that may be especially bullish for gold prices once we get the turn up. That's because JPMorgan is more likely to let gold prices rip higher than they might normally. And if JPMorgan escaped regulatory action for manipulating silver prices lower, there is little chance the bank would face any actions for letting prices soar. Also in mind is that these big long gold positions were only established because of the brutal nature of the sell-off this year. This suggests to me that this is not something that can be replicated easily or at will and may make it a unique circumstance that must be taken advantage of accordingly. In other words, I don't know how

often JPMorgan or the commercials will be able to so favorably positioned in the future as they are currently. They better make hay while the sun is shining.

More than ever, a long term approach seems to be in order. A little over two years ago we were pushing \$50 on silver, now we are pressing on \$22. Short term fluctuations aside, it comes down to what you expect to be the case two years hence. Considering the potential damage to silver production at current price levels and increased investment demand once prices stabilize and turn around, it's hard for me to imagine silver prices staying here for years. Throw in JPMorgan's and the commercials' aggressive long positioning and it becomes even harder to imagine silver prices not moving higher.

Ted Butler

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Silver - \$22.25

Gold - \$1360